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BY

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PREFATORY NOTE

The reason for this essay lies in the fact that, while selling securities through a stockbroker seller short is being constantly done, the actual way it is done is not generally known and no satisfactory description of it exists. Besides, it is the most complicated of all common commercial transactions and it is therefore interesting to see what legal rights and duties it gives rise to. Since lawyers and judges share generously in the common ignorance about this transaction, their understanding of the legal rights and duties it gives rise to is consequently far from being as correct as it should be. It is therefore in the hope that greater justice may be done to stockbrokers and their customers when they unfortunately go to law or in the legal advice they may receive that I have written this essay.

I wish to express my obligation to Mr. Maynard C. Eyre, of Messrs. Prince & Whitely, Mr. Charles G. Smith, of Messrs. Charles G. Gates & Co., and Mr. Albert M. Day, of Messrs. Counselman & Day, for their kindness in reading over this essay before it was printed.

ELIOT NORTON.

NEW YORK, October, 1907.

ON "SHORT SALES" OF SECURITIES THROUGH A STOCKBROKER [1]

WHENEVER there is any considerable amount of dealing by way of purchase and sale in any security the price of such security necessarily fluctuates. Speculatively inclined persons constantly seek to make a profit out of these fluctuations. Suppose that such a person *owns* certain securities and believes their price is going to decline temporarily. He can put himself in a position to make a profit out of this decline, if it occurs, by selling his securities; for if the decline then comes and he buys back his securities at the low price he will make the difference between what he sold his securities for and what it takes to buy them back. But suppose that the speculatively inclined person *does not own* any of the securities whose price he believes will decrease. How can he put himself in a position where he can take advantage of the fall in price he hopes for? To do so he must first borrow such an amount of securities as he wishes, then he must sell the very securities he has borrowed and deliver them to the buyer.[2] This will leave him in the position of owing the borrowed securities and of having received the price for

which he sold them. If the securities now decline in price he has more than enough money to buy back the same amount of the same kind of security as he sold, and by returning these securities [3] to the lender he can cancel the loan. If he takes these steps he will make the difference between what he sold and what he bought the securities for, less his expenses. On the other hand, if the securities sold should go up in price instead of going down he will lose money; for he will have to pay more money to buy the securities he has to return to the lender than he got for those he sold.

A transaction which has for its object the putting and maintaining of a person in a position where he can take advantage of an expected decline in the price of some security, and which is in essentials that, just described, of selling borrowed securities, is being constantly carried out through stockbrokers who belong to some Stock Exchange.[4] It is known as "selling securities for immediate delivery, seller short," or, more briefly, "selling securities, seller short," or, commonly, a "short sale." [5] To understand this transaction some knowledge must be had of the way stockbrokers who belong to a Stock Exchange do their business. As such members they are required to deal according to the rules and customs of their Exchange.[6] The main rules and customs of all American Stock Exchanges respecting dealings between their members are in brief to the following effect:

First, Of Purchases and Sales:—The members of an Exchange are allowed to deal together on the floor of the Exchange for the purchase or sale of certain kinds of securities by making verbal contracts for the payment of a fixed money price *upon* the delivery of a specified amount of securities. The times when or within which delivery may be contracted for are fixed. The delivery for which securities are usually contracted to be bought or sold is that known as "regular delivery." When securities are contracted to be bought or sold for regular delivery the rules of all Stock Exchanges fix a particular time in some particular business day *following the day* on which the contract is made before which delivery of the securities must be made by the seller. This delivery is not made on the floor of the Exchange but at the office of the purchasing stockbroker.

Since the intention of the parties to these contracts is to postpone the passing of the title of the securities contracted to be bought and sold until they are delivered and the purchase price paid, these contracts are "executory contracts of sale" in which an actual purchase and sale does not take place until the contract is performed. In spite of this, stockbrokers commonly call all contracts for "regular" delivery "purchases" or "sales," and speak of "buying" and "selling" where it would be more proper to speak of *contracting* to buy or to sell.

For every *contract* of purchase or sale which a stock-

broker makes on behalf of any person it is required that he should charge and be paid without any kind of rebate a fixed percentage of the *par* value of the securities contracted to be bought or sold. This is called his "commission."

In contracting with one another for the purchase or sale of securities stockbrokers are required when acting for those who are not members of their Exchange to contract as principals although they are in point of fact agents.[7] Consequently when any two, while acting for non-members, contract to buy and sell securities, each becomes directly bound to the other to perform his part under the terms of the contract.[8] Every Stock Exchange has established rules by which the performance of all contracts made on its floor can be conveniently carried out. In consequence of this, every such contract is understood to contain an implied term to the effect that it shall be performed according to these rules.[9]

Second, Of Loans of Securities:—The members of an Exchange are allowed to borrow securities from one another and are usually allowed to do so on any terms they like. Nevertheless, there is a customary form of written contract for loans of securities which is, with such variations as may be demanded in any particular case, almost always made use of. Its provisions are in substance as follows:

(1) In borrowing and lending securities stockbrokers

deal together as principals, even though they may be in point of fact acting as agents.[10]

(2) The loan is one of the kind which can be ended at any time by either the borrower or the lender. Consequently it is what is called a "call" loan.[11]

(3) The borrower may use the securities he borrows in any way he likes,[12] and accordingly in order to enable him to do so when he borrows stock the certificates are assigned in blank by the lender. In *effect* the title to the securities is transferred. This has led some authorities to consider such a loan as "in substance a sale."[13] This seems to be a mistake, for the parties consider the transaction a loan and in some respects the transaction is wholly unlike a sale.

(4) The borrower agrees to secure the lender by keeping in his hands at all times while the loan lasts either a sum in cash equal to the sum that would be required to buy an amount of securities equal to and of the same kind as those borrowed, which is commonly called "the market price of the borrowed securities,"[13] or, such sum and in *addition* some fixed percentage in cash of the par value of the borrowed securities. This fixed percentage is called a "margin" and does not usually exceed ten per centum of the par value of the borrowed securities. What the market price is at any moment is determined by the official record of prices on the Stock Exchange to which the borrower and lender belong.

In the first case the borrower carries out his agreement by depositing when he receives the securities their then market price with the lender. Then, whenever the price goes up the borrower is bound to add to the sum first deposited with the lender until it shall again equal the market price to which they have risen. If, on the other hand, their price goes down and they are worth less than the amount of money in the lender's hands, the borrower can draw this sum down until their market price is reached.

Exactly the same courses are pursued when the borrower agrees to secure the lender by keeping him supplied with the market price of the borrowed securities and in addition a percentage of their par value which is called a "margin." The only difference is that this additional percentage is in addition to and added on in all cases to the market price. Hence this agreement is commonly spoken of as "keeping the securities at —— per cent. above the market price," or, "keeping the margin good." Accordingly, if the securities rise in price the borrower adds to the sum in the lender's hands, and when the securities go down in price the borrower may withdraw the money deposited in the lender's hands, only provided the lender is at all times provided with the market price of the borrowed securities and the additional agreed percentage.[14]

The borrower is also bound to pay the lender whatever interest by way of coupons or dividends or otherwise and all

bonuses and accretions would have been paid to the lender on the securities he has lent had he kept them.[15] These are in practice treated as increases to the market price of the borrowed securities. The reason for this provision is that the lender is the actual owner of the securities and as such owner he is entitled to whatever they may earn by way of interest or in any other way. He has simply temporarily let another have the use of them, and since the securities can be and are disposed of by the borrower the lender would lose the interest, etc., which is paid on the borrowed securities between the date that they are borrowed and the date when they are returned and the loan cancelled unless the borrower paid an equivalent amount to him.

On the other hand, any assessment the lender would have had to pay on the borrowed securities during the continuance of the loan is a charge against him; for such an assessment is a burden adherent to ownership. In practice it is treated as a reduction of the market price.

(5) The lender agrees to pay the borrower such interest upon whatever sums of money are deposited in his hands as security as aforesaid as may be agreed upon between them. The reason for this is because the lender of the securities has the right to use the money, although it is in his hands merely as security, in exactly the same way that the borrower has the right to use the borrowed securities. Usually the rate of interest is about the

same as that which is the prevailing rate at the time for "call loans" of money.

When the security which the borrower wants to borrow is scarce the lender may demand that the rate of interest be reduced below the prevailing rate for call money, and when it is still scarcer he may demand that he be relieved from paying any interest at all. When the latter happens the security borrowed is said "to loan flat." [16]

(6) The lender charges the borrower as much as he can get for the loan. This is called a "shave," "rate" or "premium." Except where there is an unusual demand for the securities wanted by the borrower, no charge is, however, usual or possible for the lender to exact.

(7) Whenever either party ends the loan the lender is bound to return to the borrower whatever moneys he may have deposited with him to secure the loan of the securities and the borrower is bound to return to the lender securities in the same amount and of the same kind as those borrowed.[17] The lender does not get back the identical securities he lent; that would be in most cases impossible. But, since one bond is just as valuable as any other bond of the same issue and one certificate of stock is just as valuable as any other certificate for the same number of shares of the same kind, the lender is just as well satisfied to get back securities in the same amount and of the same kind as those he lent, though in different bonds or certificates,

as the lender of money who gets back the same amount of money but in different coins.[18] Bonds and shares of stock of the same kind are practically *fungible*[19] things, and it is as proper to speak of returning the borrowed securities as of returning the money borrowed in a loan of money, though in neither one case nor the other are the identical articles which are borrowed returned.[20]

Having now briefly described how stockbrokers who belong to an Exchange deal together in buying, selling, and borrowing securities, I will proceed to consider the transaction known as "selling securities, seller short."

This transaction is almost invariably carried out under a customary form of engagement of the stockbroker by the customer. It results that in almost every case this transaction is carried out in the same way and the customer and the stockbroker have the same rights as against each other. I propose to describe this mode of engagement, its legal consequences, the rights it gives to the parties, and how in point of fact a short sale is carried out under its terms.

The Order: The first step is for the customer to give the stockbroker, either verbally or in writing, "an order" to sell the securities he wishes to "go short of," for which there is a regular form.[21] This is—Sell for my account and risk—(here follows the amount and kind of securities to be sold) at—(here follows the price); and then comes some intimation that the customer is not selling securities he

owns but intends that the stockbroker should borrow for delivery to the purchaser the securities he is ordered to sell. Such an intimation would be given by the words "borrow for delivery" or "seller short." Sometimes, however, the intimation that the securities to be sold are to be borrowed for delivery is found in previous dealings of the customer and sometimes it is omitted entirely and not given until after the securities are contracted to be sold and before the time of delivery. In such case the order is exactly like the order given when a customer desires to sell securities which he owns.

Technical words are used, and technical meanings attributed, and customs have been established in the business of stockbrokers.[22] Thus, a typical order in the regular form would be written,—"Sell for my account and risk 100 D. L. & W. at 280 and borrow for delivery." So far as these customs, technical words, and meanings apply to the wording of orders in the regular form,[23] they must be described before the full meaning of such an order as this typical one can be apprehended.

(1) The word "sell" as used in an order in the regular form given to a stockbroker who is a member of a Stock Exchange is taken to mean "contract to sell on the Stock Exchange to which you belong according to its rules and customs."[24]

(2) The words "for me" or "for my account" as used in an order in the regular form are taken to mean that the

contract the stockbroker is directed to make is to be made for and on behalf of the customer.

(3) The words "at my risk" as used in an order in the regular form have the customary significance that the customer assumes the risk of any failure to perform on the part of the stockbroker or stockbrokers with whom his stockbroker contracts, and that he does not require the latter to guarantee in any way that the contract or contracts which he makes will be performed by the stockbroker or stockbrokers with whom he contracts.[25] If these words are omitted in an order in the regular form, as they may be, they are implied by force of custom.

(4) When an order in the regular form does not state a particular delivery for which securities are (to be contracted) to be sold, it is then taken to mean that they shall be (contracted to be) sold for "regular" delivery.

In selling securities "seller short" the intention is to make a present sale of securities, hence the securities are sold for "regular" delivery, and because of this custom nothing need be said about the delivery in the order.

(5) A large number of abbreviations of the full names of corporations and for various kinds of securities are customarily used among stockbrokers. When any of these abbreviations are used in an order in the regular form they are taken for what they stand for to stockbrokers.

(6) Where an order in the regular form simply states a number before the name of a corporation or its custo-

mary abbreviation, as "Sell for my account and risk 100 Ontario and Western," the number in question is taken to mean the number of shares of the capital stock of the corporation named which are to be (contracted to be) sold. If the capital stock of the company is divided into preferred and common stock the order should of course specify which kind is intended, but if this should be neglected the order will be taken by custom to refer to common stock.

(7) Bonds and shares of stock are contracted to be bought and sold on the floor of a Stock Exchange for so much for each hundred dollars' worth of the par value. Hence, when an order in the regular form simply states a number *at* which a number of bonds or shares of stock is to be sold, as "Sell for my account and risk 100 D. L. & W. at 280," the number in question is taken to mean the number of dollars or price for which each hundred dollars' worth of the par value of the bonds or stock shall be (contracted to be) sold; subject, however, to the following custom:

That where a particular price is stated in an order in the regular form the words "or better" are read in after it, which mean that the price stated is the price at which the securities shall (be contracted to) be sold unless a better, *i.e.*, a higher, price is obtainable, in which case they shall be (contracted to be) sold at such higher price.

(8) Where no price is stated in figures in an order in the

regular form, but the securities are ordered to be contracted to be sold "at the market price," or, "at the market," it is taken to mean that the securities are (to be contracted) to be sold for the best price, that is, the highest, obtainable.[26]

(9) Where an order in the regular form does not state anything at all about the price for which the securities are (to be contracted) to be sold, the order is taken to mean that the securities shall be (contracted to be) sold "at the market price," the meaning of which has just been explained.[27]

(10) The intimation that the customer desires the stockbroker to borrow the securities he is ordered to sell for delivery, however briefly given, as, for instance, by such phrases as "borrow for delivery" or "seller short;" means, when given its full significance, that the customer desires the stockbroker, in case he contracts to sell the securities he is ordered to sell, to borrow securities in the same amount and of the same kind as those he is ordered to sell and deliver these according to the rules of his Stock Exchange under the contract or contracts to sell which he may make.

Interpreting according to these customs, technical words and meanings the order taken as typical, "Sell 100 D. L. & W. at 280 and borrow for delivery," it becomes, "I order you to contract to sell for regular delivery for me and at my risk on the Stock Exchange of which you are a

member, according to its rules and customs, 100 shares of the stock of the Delaware, Lackawanna & Western Railroad at 280 dollars or better for every hundred dollars' worth of the par value of the shares, and I further order you to borrow 100 shares of the same stock and deliver these according to the rules of your Stock Exchange to the purchaser or purchasers under the contract or contracts of sale."

The Legal Nature of an Order: Stockbrokers form a particular class of semi-public brokers, and as such hold themselves out as ready to act as agents[28] for their employers, who are called "customers" or "clients." Obviously an order is a proposition to vest the stockbroker with an agency. As between the principal and the agent the scope of every agency depends primarily on the principal's intent. I will assume that the customer's intent in giving an order is that it should be interpreted according to the customs, technical words, and technical meanings which have been stated.

This assumption is made in order to avoid any discussion of the legal rules governing the interpretation of orders by courts of law where the customer's intent is in dispute. The law is in by no means a satisfactory condition respecting how far such customs as have been described may be proved in evidence and their effect upon the interpretation of an order when so proved.[29] It follows that a stockbroker's only safety lies in bringing these

customs to the customer's knowledge and having the customer clearly express the full significance of his order. This is all the more necessary where the customer is, as is usual, more or less ignorant of these customs. Making this assumption, an order in the regular form bears the significance stated above and will be found to contain:

(1) A proposition to make the stockbroker the customer's agent with authority to do three things, as follows,

(a) to contract to sell, according to the rules and customs of the Stock Exchange of which the stockbroker is a member, the securities stated in the order on the terms there stated. Since this authority is "to contract," it permits the stockbroker making as many separate contracts with one or more other stockbrokers as may be necessary to sell the securities stated in the order;

(b) to borrow the securities necessary to deliver under the contract or contracts made under the authority to contract to sell;[30] and this authority being simply "to borrow" permits the stockbroker to borrow from one or more lenders as he sees fit;

(c) to perform the contract or contracts made under the authority to contract to sell by delivering the borrowed securities according to the rules of the Stock Exchange to which the stockbroker belongs, and by receiving at the same time the purchase price from the buyer.

The authorities to contract to sell and to borrow are

clearly expressed in the order. The authority to perform must be implied, but the ground for its implication is solid, and is that the customer must be held to propose to authorize the necessary consequences of what he expressly proposes to authorize, and personal performance by the stockbroker of the contract or contracts of sale he makes is a necessary consequence of making it or them according to the rules and customs of his Stock Exchange, as is expressly proposed he should do. Besides, the authority to borrow is given only in order that the contract or contracts of sale may be performed.

(2) An implied offer by the customer that, if the stockbroker becomes the customer's agent as proposed by the order and in consideration of doing so,[31] the customer will reimburse and indemnify him for all outlays, expenses, and losses necessarily or reasonably incurred in so acting as agent. Such an offer is implied in almost every proposition to confer an agency.[32]

(3) An implied offer by the customer to pay the stockbroker a commission in accordance with the requirements of the rules of his Stock Exchange.[33]

These requirements are that the stockbroker shall be paid a commission for every contract he makes on the floor of the Stock Exchange to which he belongs, which is a fixed percentage of the par value of the securities contracted to be bought or sold. Hence the customer's implied offer is to pay the stockbroker the usual com-

mission in consideration of and on the making of any contract or contracts of sale he may make to carry out the order. Accordingly, this offer remains as made, and unaffected by anything the stockbroker may do, until he has actually *contracted to sell* the securities.[34] Then, by the performance of what the customer offered to pay for, the customer's offer to pay a commission ripens into a promise to do so. In this way a contract springs into existence binding the customer to pay the fixed commission. This contract is of the unilateral or executed variety.

The Taking of an Order: Where a proposition to confer an authority is made all that is required in law to create the relation of principal and agent between the proposer and the person to whom the proposition is made is that the latter should consent to the proposition. Hence, after an order is given to a stockbroker the next step is for him to decide whether he will refuse it or consent to it. If he does not wish to refuse it, as he may in any case,[35] he will express in some way by words or acts his consent or willingness to undertake what he is ordered. Such *an expression of willingness* is called "taking" the order. This expression of willingness, this consent to the proposition made him, need not necessarily be communicated by the stockbroker to the proposer,—it may be inferred from his conduct. So, too, a refusal to consent to a proposition to confer an agency need not be communicated but can be left to be inferred.[35] But since

it is very easy, except in clear cases, for error to arise in inferring what a stockbroker means in the case of his remaining silent when an order is given him the wiser course is for him always to *communicate* his consent or refusal to his customer. This is practically essential in the case of an intended refusal, for from silence after receiving an order consent rather than refusal will almost invariably be inferred. The practical wisdom of notifying the customer that an order is refused has led some stockbrokers to think they are "bound" to do so, and they act accordingly; but the law is clearly as stated, and there does not seem to be any established custom of notifying a customer of the refusal of an order. In communicating his refusal or consent the stockbroker can express the one or the other in any way he likes.

As a condition of taking an order a stockbroker almost invariably demands a "margin"[36] from the customer and will not take the order until it is deposited with him by the customer. But the margin is not absolutely necessary and may not be asked for, in which case the whole engagement of the stockbroker consists of the giving and the taking of the order. Assuming this to be the case and leaving the margin and its effect on such an engagement to be subsequently stated,[36] I will state what is the legal effect of the taking of the order.

The Legal Effect of "Taking" an Order: This is to constitute the stockbroker the customer's agent, and to vest in

him the authorities proposed by the order, and also to turn the customer's offer to indemnify the stockbroker into a promise to do so; but it has no effect upon the customer's offer to pay a commission. That remains an offer until the securities are contracted to be sold.

The Legal Effect of the Engagement: It follows that the legal effect of the engagement of a stockbroker, consisting in the giving of an order and the "taking" of it, is to create an agency coupled with an offer to pay a commission and a promise to indemnify the stockbroker.

It is to be carefully noticed that in this regular form of engagement a promise on the part of the stockbroker to carry out the order [37] or to do anything except to act as the customer's agent cannot be found. Yet there are to be found many statements that the stockbroker is bound [38] or agrees to do this or that, and pleadings are being continually drawn as if he were bound or had agreed to do something. In point of fact, stockbrokers will rarely, if ever, assume the risk of promising that an order will be carried out.

Assuming now that a stockbroker has been engaged by his taking an order like the one given above as typical, I will state according to what legal principles and how as matter of fact he must thereafter act to carry out correctly his engagement.

Of the Carrying Out of an Order: The relation between

the customer and the stockbroker created by the usual engagement being that of principal and agent, the principles of the law of agency govern its carrying out. If in any case the stockbroker carries out the order according to the intent of the customer, the customer is bound. This is the meaning of the stockbroker having authority. If, however, the stockbroker fails to carry out the order according to the customer's intention, the customer is not bound.[39] In such case he need not take any steps to assert this.[40] On the other hand, if he chooses to, he can ratify what has been done contrary to his intention.[41] Ratification rests on the consent of the customer to be bound. Therefore, he should as a matter of precaution repudiate anything done contrary to his intention in order that his silence may not be taken and used as evidence of consent.[42]

Another principle of the law of agency is that the law requires of one who undertakes an agency that he should exercise due care in and about what he is entrusted to do, and to act in good faith toward his principal.[43] If he fails in either direction he will be liable for damages.

The degree of care which a stockbroker must show is to be measured by the standard of care which a faithful and intelligent stockbroker thoroughly versed in his business[44] would show. It is not to be measured by the degree of care which one not a stockbroker would show, or by that degree of care which is customary or which stock-

brokers usually give,[45] unless such degree of care is that which an intelligent, faithful, and competent stockbroker would show.

The duty of showing good faith is very stringently enforced.[46] In doing so, judges incline to lay down general rules of conduct rather than to decide each case on its merits. Thus the rule is established and enforced without exception that a stockbroker cannot sell to or buy from himself,[47] from his clerk,[48] or from a firm or corporation of which he is a member,[49] and this without proof of fraud,[50] and even in case where the price obtained for or given by the customer is as good or better than would otherwise have been obtained or paid.[51] There is no established custom which would justify stockbrokers in violating this rule of law.[52]

These are the main principles of the law of agency which govern the carrying out of the order.

How, now, as a matter of fact, does the stockbroker carry out the order, assuming the customer's intention to be that the order shall be interpreted according to the customs, technical meanings, and technical words already stated? He is authorized first to contract. This authority is qualified by two customs. Before stating them it is necessary to explain that the "execution" of an order consists only of the *contracting to sell* the securities ordered upon the terms of the order, and an order is said to be "executed" when this is done.[53] In other words, the

"execution" of the order is the carrying out of the authority to contract to sell. These two customs are:

(1) An order in the regular form to sell securities can only be "executed," if at all, on the day it is given, unless it is expressly stated in the order that it is "good" for a longer period of time or for some particular period of time.[54] In this case the order is usually made "good till countermanded," which is usually abbreviated when written to G.T.C.

(2) There is implied as a term or condition proposed by an order in the regular form that the stockbroker shall try to "execute" the order as early in the time for which it is "good" as it is possible for him to do in accordance with the rules and customs of the Stock Exchange to which he belongs.

Assuming that the customer's intention is that these two customs should apply to the order it follows that the stockbroker's first step is to try to execute the order at the earliest possible moment in the time for which it is good. If he is unable to at once he must continue trying throughout the period for which the order is good. If he neglects this duty he will be liable in damages.

Now, unless he carries out the terms of the order exactly the customer will not be bound, and the stockbroker will presumptively be liable for want of care. For, unless given discretion,[55] the stockbroker cannot vary[56] in any particular from the terms of an order, even where he

benefits[57] the customer by so doing. Good intentions on the stockbroker's part are no excuse in law for failure to carry out orders. Hence he must try to contract to sell according to the rules and customs of his Stock Exchange the exact amount of the particular kind of security stated in the order at the price or better, if any is fixed, or, if no price is fixed, at the highest market price for regular delivery. If the stockbroker succeeds in contracting to sell as he is ordered to he is said to have "executed" the order, and the order is said to be or to have been "executed."[58] And this is so although the actual performance of the contract or contracts by the delivery of the securities and the payment of the price has yet to come.

In spite of the maxim, *Delegata potestas non potest delegari*, custom permits a stockbroker to delegate the execution of an order to some other stockbroker.[59] This custom does not, however, apply where reliance is expressly or impliedly put in a particular stockbroker's skill to execute an order. The stockbroker can also delegate to his clerk the doing of the acts constituting the performance of the contract or contracts made.[60] Where, however, anything is left to the stockbroker's discretion he must exercise his personal judgment.[61]

In executing an order the stockbroker can make one contract or as many contracts (his authority being to contract) with the same or different stockbrokers as may be necessary or advisable, provided that the total

amount of securities contracted to be sold is the amount stated in the order. No custom exists allowing a stockbroker to contract to sell a less amount of securities than he is ordered to in a case where no discretion is given to him to do so. This discretion is, however, usually given either expressly or by implication with all orders to sell more than one hundred shares or ten bonds, and the number of shares or bonds stated in the order is in such case treated as a limit to be reached if possible.[62] Where such discretion is given, the order is said to be "executed" for as many shares or bonds as are contracted to be sold.

The Commission: When the stockbroker has contracted to sell according to the terms of the order the customer's offer to pay him a commission according to the rules of the Stock Exchange to which the stockbroker belongs ripens into a promise to do so. The customer is not bound to volunteer to pay it. He can wait until the stockbroker asks him for it. The stockbroker does not usually demand it of the customer at this time but charges it against him and waits for it until he accounts to the customer.

The Notice: There is a custom that the stockbroker, as soon as he conveniently can after "executing" an order, shall give or send to the customer a written notice of what he has done.[63] If the notice is sent to the customer, it must be sent in such a way that knowledge of its contents can be imputed fairly to him. To do this, it would

be held in most jurisdictions that mailing to the customer the notice postage paid and properly addressed or leaving it at his business office or, if he has no office, at his home was sufficient, without proof that the notice reached him, where there was no evidence that it did not reach him. In the case of Granite Bank v. Ayers, 33 Mass. 392, Chief Justice Shaw laid down the rule that "all notices at one's domicile, and all notices respecting transactions of a commercial nature at one's known place of business, are deemed in law to be good constructive notice, and to have the legal effect of actual notice." Subject to this rule of law, the question whether the customer was notified or not is a question for the jury.[64]

The stockbroker need not follow any particular form in this notice. There is, however, a customary form which is almost always used. This states exactly what kind of contract or contracts the stockbroker has made, the date on which it or they were made, and gives in addition the name of the stockbroker or stockbrokers with whom the contract or contracts of sale has or have been made. As regards the wording of these notices, the same customs, technical words, and technical meanings which are used in the wording of orders in the regular form are made use of in the same way, mutatis mutandis. Since these customs have been stated, they need not be repeated here. A notice which would be typical would read:

JUNE 26TH, 1906.

To JOHN WARD, ETC.,

"I have this day sold for your account and risk 100 D. L. & W. at 185 to Brown & Co.

(Signed) "E. C. SMITH."

Where it is the customer's intent that the custom of giving such a notice should apply the law will enforce it as a term of the stockbroker's agency and will require that the notice shall be given or sent. Thus it has been held that a failure to give this notice was such "negligence" on the part of the stockbroker as to preclude him from recovering his commissions.[65]

The Loan: After the securities have been contracted to be sold and before the time for the delivery of the securities under the contract or contracts of sale the stockbroker borrows[66] under the authority to borrow contained in the order the securities which are required to make delivery.

The Delivery: When the time of delivery of the securities under the contract or contracts of sale comes, the stockbroker delivers according to the rules of his Stock Exchange the securities he has borrowed to the stockbroker or stockbrokers with whom he has contracted. Thus the transaction is in effect a sale of the borrowed securities. On so delivering the securities he must receive the purchase price agreed to be paid. All this is done under his authority to perform contained in the or-

der. When it is done the sale is complete.[67] The stockbroker credits the customer on his books with the amount of the purchase money received and charges him with the amount of his commission. That is, this money is treated exactly as if it had been securities that the customer owned that had been sold. The stockbroker does not pay to the customer the purchase price less the commission, but he holds it for purposes which will be shortly explained.

The Terms of the Loan: Having now finished describing the sale of the securities it is necessary to revert to the loan and consider its terms and its consequences.

The stockbroker may borrow the securities necessary to deliver from any person and upon any terms subject to the following restrictions which are established by custom:

(1) The loan must be made by the stockbroker in his name as borrower.[68]

(2) The stockbroker can make no charge to the customer for procuring the loan.

(3) The stockbroker cannot charge the customer with any payment to the lender for the loan beyond the prevailing rate or premium, if any, at which similar loans are at the time being made.

(4) The loan must be one that the stockbroker can end at any time.[69] It follows that as the stockbroker has this right the lender will also exact it for himself.

(5) The stockbroker cannot call on the customer to secure the loan.[70]

While these restrictions are the only limitations upon the stockbroker's authority to borrow and while the stockbroker may borrow of any person, he almost invariably borrows either from some fellow member of his Exchange upon the usual terms [71] for loans which have been stated, or, from himself acting as agent for some other person. Thus it is very common for the stockbroker to lend securities he is "carrying" for a customer.[72] This right is given to him by custom. Sometimes a stockbroker will lend securities he himself owns. This is a violation of the rule of law that an agent cannot deal as a principal with his principal and I do not know that any custom exists to justify it.

The Maintenance of the Loan: After the loan has been made the customer is in such a position that if he can procure securities equal to and of the same kind as those sold but at a lower price and have the loan cancelled with them he will make a profit. This is the position the customer intended to get into when he engaged in this transaction.[73] It is obvious that the customer will remain in this position so long as the loan lasts. Unless he can secure the lasting of the loan for some time it would be folly for him to engage in this transaction, since it is uncertain when he will be able to procure the securities at a lower price. This he secures in the following way: Since the stockbroker is the only person that can maintain the loan (inasmuch as he makes it in his own name) and since

the purposes of the customer require it, the law will find in the authority to borrow *an implied authority to maintain the loan.* The great rule of agency of course applies to this authority—the stockbroker must use care and act in good faith to maintain the loan.[74] Speaking broadly, he will have done so if he gives the lender no cause to end the loan.

The stockbroker is, however, not required to exercise due care and good faith to maintain the loan *indefinitely.*[74] For after the loan has been maintained for a reasonable time he has the right to buy for or on account of the customer and upon notice to him securities in the same amount and of the same kind as those borrowed, return them to the lender, and thus bring the whole transaction to an end. This right will be considered in detail further on.

The stockbroker also has authority to substitute at any time one lender for another.[75] In this case the first loan is cancelled with the securities of the new lender, who steps into the shoes of the earlier lender. This authority is established by custom and finds its reasons in the lender's right to end the loan at any time and because it may serve the convenience of the stockbroker. In its exercise the stockbroker has of course to show due care and good faith. Between the customer and the stockbroker successive loans are treated as one loan,[76] however many substitutions there may be. Thus in considering

the stockbroker's right to end the transaction after a reasonable time, the time is computed from the making of the first loan without regard to how many subsequent substitutions there may have been.

Connected with the maintenance of the loan is the authority, which the stockbroker has, to pay to the lender on demand, while the loan continues, the premium at which at the time similar securities may be lending for in the open market. This authority is also established by custom and finds its reason in the lender's right to end the loan, which he would undoubtedly exercise if he were not paid the premium he could get in case he should loan his securities to somebody else. This authority must of course be exercised with due care and good faith. It exists as well where the stockbroker lends the securities himself as agent for some third person as where he borrows the securities from a fellow member of his Exchange.

The Stockbroker's Security: In making the loan in his own name the stockbroker incurs in all cases a personal obligation to the lender to return to him the securities he borrows and to pay him all interest by way of coupons or dividends or otherwise and all bonuses and accretions which would have been received by the lender during the time of the loan had he retained the securities. It is obvious that the stockbroker needs security for incurring this liability on behalf of the customer.

Furthermore, where the stockbroker borrows from a fellow member of his Exchange he will almost invariably be required, so long as the loan lasts, to keep the securities at the market or at some percentage over and above the market price.[77] Against this obligation also he needs security; and as he may have, because of the securities rising in price, to be constantly paying money to the lender, it must be arranged that the security shall increase according to his needs.

These various matters of security are arranged for by leaving the purchase money received from the sale of the securities in his hands and by the margin exacted from and put up by the customer.

The Margin: It has been said that as a condition of taking an order the stockbroker usually demands the deposit upon certain fixed and customary terms of a margin, which is a certain percentage in cash of the *par* value of the securities to be sold.

It is possible to carry out a short sale of stock without a margin if the stockbroker is willing to do so. There is, therefore, no custom or rule of law which compels the customer to deposit one unless asked to. Hence if the stockbroker wants to have a margin he must expressly stipulate for one. It is customary for the stockbroker to demand that the margin shall be deposited at the time he takes the order. But, since he must return it at once if he fails to carry out the order, he may be satisfied merely

to have the customer promise that in the case the order is executed he will deposit one.

The amount of the margin wanted must also be stated by the stockbroker. The amount of the margin asked for is usually ten per centum in cash of the par value (not of the market value, as is sometimes thought) of the securities to be sold, but it may be more or less.[78] Stocks, bonds, or anything of value may be deposited with the stockbroker, if he is willing, in place of cash as a margin. In reality, however, such securities are not, strictly speaking, a margin, but form a pledge[79] by the customer to the stockbroker for the amounts of money which would otherwise be charged against and paid out of the customer's margin and which the stockbroker now pays with his own money.

The demand for margin is so usual and has been complied with in so many cases that the terms on which it is deposited are fixed, in the absence of any special agreement, by custom. They are as follows:

(1) The stockbroker is bound in case he fails to "execute" the order to return the margin, if already deposited with him, without any deduction whatsoever to the customer; and if, as is sometimes the case, the margin has not been deposited but the customer has agreed to deposit it on the "execution" of the order, then in case the stockbroker fails to "execute" the order the customer is of course relieved from depositing it.

(2) The stockbroker has the right to charge against the margin and pay out of it everything he can rightly impose upon the customer (as, for instance, his commission), and every disbursement he makes on his account (as, for instance, all sums paid the lender),[80] and also to treat the margin as being reduced by just as much as the securities sold gain at any time in total price[81] over the price they were sold at.[82]

Whenever the margin is reduced in any of these ways the customer is bound on demand by the stockbroker to make up his margin to the original percentage agreed upon.[83] When the customer does so, he is said "to make his margin good," and if he does so regularly he is said "to keep his margin good." It is to be noted that the customer is under no duty "to make" or "keep his margin good" unless *called upon* to do so. Hence he need not look after its condition himself, and can suffer it to be impaired without any consequences to himself until called upon "to make it good." Only by special agreement can the customer be bound to make the margin good, in case of any depletion, without any demand.

(3) If the customer fails to make his margin good within a reasonable time after being properly called upon to do so, the stockbroker has the right to buy for and on account of the customer securities in the same amount and of the same kind as those borrowed, and to end the loan with them, and charge any loss incurred in so doing

to the customer. This right will be considered more fully toward the end of this essay.

(4) Since the customer's obligation is to keep on demand his margin *at* a certain percentage, it follows that if, after a margin has been reduced by a rise in the price of the securities sold and the customer has made it good, the price of the securities falls and recedes the customer can draw down his margin and take as much back as the securities have receded in total price, and can continue to do this until he reaches the amount of his original margin. To illustrate, suppose a margin of $1,000 is put up on a sale of 100 shares at par. Then the price rises to $105 per share. The margin is reduced by $500 and the customer makes it good. Then the price goes back to $103 per share. In such case the customer can withdraw $200 of the $500 with which he previously made his margin good. If the price then goes back to par the customer can withdraw $300 more.[84]

(5) The stockbroker must be ready at all times to account to the customer for all the margin deposited in his hands. Since the customer's margin is a "fund" deposited with the stockbroker for certain fixed purposes only, it partakes of the nature of a trust fund, and forms no part of the assets of the stockbroker, and his creditors have no claim upon it. Still there is no special law, custom, or rule compelling the stockbroker to keep it separate from his other funds, nor in practice does he ever do so.[85] Thus, since

it cannot usually be traced and separated from these other funds, the confusion which would ensue in case of failure of the stockbroker would probably operate so as to preclude the customer having much, if any, advantage over other creditors so far as his margin was concerned.

These are the customary terms on which the margin is deposited. It follows that in law an agreement between the customer and the stockbroker will be implied out of the demand for margin and the customer's depositing it that the customer and stockbroker shall be severally bound to comply with these customary terms. And it is to be noted that this agreement does not change the legal effect of the engagement of the stockbroker created by the giving and taking of the order, but only adds thereto a collateral arrangement of security.[86]

It has been said that the purchase money and the margin furnish security to the stockbroker from liability on his obligations to the lender. It is now in order to consider in what way they do.

Suppose the stockbroker has himself lent securities as agent for some third person. He keeps the original purchase price received on the sale of the securities in his hands. Besides, he also starts with the margin intact in his hands, and with the right to have it made good when in any way depleted. If it is kept good the stockbroker will always have in his hands the original market price of the securities and the margin, and will receive besides sums

equal to all the interest, bonuses, and accretions which are paid on the securities he lent during the continuance of the loan. In this way he has always in his hands more than funds enough to make good to the owner of the securities those that were lent, and all interest, bonuses, and accretions he would have received if they had not been lent.

Where the securities are borrowed from a fellow member of the Exchange the stockbroker borrowing the securities on the usual terms will be bound to keep the securities at the market price or at some percentage over the market price. He can easily do this by means of the money received on the sale of the securities and the customer's margin. For the money received on the sale of the securities should equal the market price at the time of borrowing, and then any percentage above that and all sums required to be thereafter paid to the lender are provided for by the customer's margin,[87] for, as will be seen by comparison of the terms of the loan and those of the margin agreement, the margin is reduced whenever and by as much as the money in the lender's hands is, and the amount which in such case must be paid to the lender is the same amount which the customer has to pay to make his margin good.[88] It follows that if the stockbroker does this faithfully the lender will receive from time to time sums equal to all interest, bonuses, and accretions which he would have received had he retained the securities,

and will always have in his hands at least the market price of the securities lent, however it may fluctuate, and also, if he has demanded it, a percentage over and above this.

In this way then the stockbroker's liability to the lender is secured.

Of Ending the Transaction: As already stated, this transaction contemplates that the loan will sometime be paid off. When it is, the customer's opportunity to make a profit will no longer continue and the end of the transaction will be reached.

Of the Customer's Right to End the Loan and the Transaction: At any time after the loan has been made the customer has the right to have the loan closed and the transaction brought to an end.[89] It is to enable him to exercise this right that the loan is required to be made so that it can be ended at any time. Though the loan is made in the stockbroker's name yet it is made for the customer, and consequently this right is the right of one of the principals[90] in a call loan to bring it to an end whenever he likes. Inasmuch, however, as the stockbroker makes this loan in his own name, this right can only be exercised through his intervention. To meet this necessity the law will find in the stockbroker's agency to borrow in his own name an implied expression of willingness to act as the customer's agent in closing the loan.

To exercise this right all the customer has to do is

to provide the stockbroker with the securities requisite to satisfy the loan and direct him to close the loan with them. Since the stockbroker is the customer's agent to close the loan, he must obey this direction and must act with due care and good faith. He must promptly notify the lender of his desire to end the loan; then he must give the lender the securities provided him and receive from him whatever moneys may be in his hands as security for the loan. When this is done his next duty is to account to the customer.[91] Then the whole transaction will be at an end.

The way the customer usually gets and intends from the beginning of the transaction to get the securities needed to close the loan is to buy them. And since it is obviously more convenient to do so through the stockbroker who originally sold them the customer almost invariably does so. The stockbroker is engaged to carry out a purchase of this kind in the same way and his engagement has the same legal effect, the same consequences, and is carried out the same way as in the case of any outright purchase of securities through a stockbroker,[92] except that the customer is not called upon to provide the money for the securities bought; the stockbroker pays for them, inasmuch as there is to the customer's credit on his books and held by himself or the lender the proceeds of the securities that were sold, and the customer's margin.

I will describe very briefly how this purchase is usually

effected. The first step is for the customer to give an order, for which there is a regular form,[93] to buy the securities in the same amount and of the same kind as were previously sold. Since these securities when bought are intended to be used to cancel the outstanding loan the order is accompanied or followed by some direction that they are to be so used. The order, when in the regular form, is worded according to customs, technical words, and technical meanings which are the same as those previously stated,[94] substituting the word "buy" in place of the word "sell."

The legal significance of this order to buy, leaving out of account the added direction for the use the securities are to be put to when bought, is exactly like that of any order to buy in the regular form.[95] Hence the legal effect of the stockbroker's engagement created by taking[96] such an order is in brief to make the stockbroker the customer's agent with authority (a) to contract to buy according to the rules and customs of the Stock Exchange of which the stockbroker is a member the securities stated in the order on the terms there stated, and (b) to perform the contract or contracts he makes. This agency is also accompanied by an implied unilateral offer by the customer to pay a commission to the stockbroker according to the rules of his Stock Exchange, and a promise by the customer to indemnify the stockbroker.

The stockbroker's authority to contract is subject to

the two customs previously stated on page 24 substituting the word "buy" in place of the word "sell." The stockbroker must consequently try to carry out this order at the earliest moment he can in the time it is good for. If he succeeds, the order is said to be executed and the stockbroker becomes entitled to his commission. On the execution of the order the stockbroker is bound by custom to give or send a written notice of what he has done to his customer. Subsequently, on the delivery of the securities he has contracted to buy, he pays for them, and charges the customer with the purchase price.

Having received the securities, the stockbroker proceeds to fulfill the customer's direction and to end the loan. If he himself, as agent for some third person, lent the securities, there is practically nothing for him to do except to make the proper entries in his books. If he borrowed them from some lender he must call the loan, deliver the securities he has bought, and receive from the lender whatever moneys he has in his hands as security for the loan. In either case after the loan is closed his duty is to account to the customer.[91] In doing so the customer is credited, on the one hand, with the money received from the sale of the securities, and with all the money he has deposited as margin; on the other hand, he is debited with the stockbroker's commission on the sale, with all bonuses, accretions, interest by way of dividends, coupons or otherwise paid on the borrowed securities, with all

premiums paid to the lender, with the money which it cost to buy back the securities, and with the stockbroker's commission on such purchase.[97] In every case where the customer has kept his margin good there will be a balance in his favor, and if the money which it cost to buy back the securities is sufficiently less than the money received on the sale of the securities to cover all the sums charged against the customer, including commissions and all sums paid the lender for premiums and bonuses, accretions, and interest paid on the borrowed securities, there will be a profit in addition. *This is the regular way of ending the whole transaction.*

Besides this way of ending the transaction the customer also has the right[98] at all times when his account does not show that he is indebted to his stockbroker to order him "to transfer his account" to another stockbroker. This involves a new stockbroker taking the place of the first stockbroker by his making a new loan and then giving the newly borrowed securities to the first stockbroker who will pay off the loan which he made with them, account to the customer, and turn over the moneys in his hands to the new stockbroker, who will use them as the first stockbroker did. This is, of course, equivalent to the ending of the transaction with the first stockbroker and the beginning of a new one with the new stockbroker without a preliminary sale.

Of the Stockbroker's Right to End the Loan and the

Transaction: The stockbroker has a right in two instances to buy for account of the customer securities equal in amount and of the same kind as those borrowed, give them to the lender, and thus end the loan and the transaction without any order or direction of any kind from the customer.

(1) It has already been stated that the customer is bound on demand by the stockbroker to keep his margin always at the percentage of the par value of the stock originally agreed upon. Hence, whenever the margin is reduced below the original percentage, the stockbroker has the right to make demand upon the customer for more margin.[99]

This demand is usually in writing, but it may be verbal.[100] Whether written or verbal, it need not be in any particular form;[101] all that is necessary is that it should be of such a nature that the customer will clearly understand what is wanted by the stockbroker. It should state the exact sum of money wanted to make up the margin to the original percentage agreed upon,[100] and must be made upon the customer personally, though it would probably be held sufficient to make it in writing at his regular place of business if he cannot be honestly found. An exactly similar demand is made when margin is wanted by a stockbroker who is "carrying" securities for a customer on a margin, and hence decisions on the necessity of making the demand, on the kind of demand required, and how it should

be made where stocks are being carried apply to cases involving corresponding questions in connection with short sales of securities.[102]

The customer has the right to have a reasonable length of time to comply with a demand for more margin.[103] On the trial of Cameron vs. Durkheim,[104] the Court charged—"What is a reasonable time is usually a question of law; in the absence of a special contract defining what shall be a reasonable time, the party who is to make the payment or perform the obligation is entitled at least to the usual bank hours of the day within which to comply." If by this the Court meant to lay down an inflexible rule of law as to what was the least amount of time which could be considered reasonable, the Court was in error. No rule can be laid down as to what constitutes a reasonable length of time to comply with a demand for margin. Each case must be judged by itself in the light of its own circumstances. Nor is "what is a reasonable time" a question of law, but it is a question of fact for the jury.[105] Decisions on the right of the customer to have a reasonable length of time to comply with a demand for more margin and on what is a reasonable length of time to comply with such a demand in cases where a stockbroker is "carrying" securities on a margin are of course in point.[106]

At the expiration of a reasonable time *after the demand* for more margin the stockbroker has the right,[107] provided

the customer has failed meanwhile to comply with the demand or to order the stockbroker to close the transaction, to buy for and on account of the customer securities equal in amount and of the same kind as those previously sold, and return them to the lender and close the transaction.

The Notice of Sale after Demand for Margin: As a condition precedent to the exercise of this right the stockbroker is required[108] by both law and custom to notify the customer that he is going to buy in the securities sold on account of the customer's failure to keep his margin good and is going to close the transaction. In giving this notice no particular phraseology or form is customary or necessary. It need not state where or when the stockbroker is going to buy the securities with which to close the loan. All that is necessary is that the notice should be such a notice that the customer will clearly understand that the stockbroker is going to buy back the securities previously sold, give them to the lender, and close the transaction on account of the customer's default in not furnishing margin. Unlike the demand for margin, which must be made personally on the customer, the notice need not be served personally on the customer, but may be left in writing at his office or at his house, if he has no office.

It seems to be the law that a reasonable length[109] of time must be allowed after the notice has been given before the stockbroker can proceed to buy the securities and close

the transaction. There can be no doubt that this reasonable length of time is not any longer than the period which must be allowed to comply with a demand for more margin. For this reason the notice should always be joined with a demand for margin. If not, the period of time between the making of the demand and the giving of the notice is wasted. Where the notice is joined with the demand and the demand is complied with or the customer orders the stockbroker to close the transaction the notice of course falls; if, on the other hand, the customer does not order the stockbroker to close the transaction and the demand is not complied with, then, as soon as a reasonable time has elapsed from (the making of the demand and) the giving of the notice, the stockbroker should proceed to buy back the securities and to close out the transaction.[110]

This right of buying back the securities and paying off the loan with them is established by custom,[111] and the custom is that in exercising this right the stockbroker must close the transaction exactly in the same manner as if he had received an order from the customer to buy the securities needed to repay the lender at the "market price" and close the transaction with them. In law this right is equivalent to an authority from the customer and consequently the stockbroker in exercising this right is in effect the customer's agent and the principles of the law of agency apply generally.

(2) The stockbroker has the right,[112] after he has main-

tained the customer in the position of being short of the securities sold for a reasonable time after their sale, to end the transaction even if the customer's margin is at the original percentage agreed upon.

This right is the right or implied authority every agent has to end his agency after a reasonable time.

No rule can be laid down for determining what a reasonable time in this connection is. Each case must be decided as it arises by all its circumstances. What is fair to both parties should be the controlling factor. In the ordinary case the reasonable period in this connection is rather of weeks or even of months than of days. And while the stockbroker should not be bound indefinitely to maintain his customer, yet it should be remembered that he is running no risk[113] and can well afford to treat his customer generously in the matter of time. Still all the circumstances of each case should be considered.

In the event of his wishing to exercise this right the stockbroker is first bound to notify[114] the customer of his desire to end the transaction. This notice may be by word of mouth or in writing. When in writing, this notice need not be served personally upon the customer but may be left at his office, or at his house if he has no office. In this notice the stockbroker usually requests the customer to order him to end the transaction. The object of inserting such a request in the notice is to secure, if possible, an order to buy from the customer and thus gain an *ex-*

press authority for the purchase of the securities with which to pay off the loan and end the transaction.

The stockbroker's course now varies according to what the customer does.

(1) The customer can order the stockbroker to transfer the whole transaction to another stockbroker.

This is in effect ending the transaction and carrying out the stockbroker's wishes.

Before this can be done the customer has of course to secure another stockbroker who is willing to assume the transaction for him. If he can do so, then the transaction is closed out with the first stockbroker and assumed by the new stockbroker in the way already described.

(2) The customer can order the stockbroker to buy back the securities sold, return them to the lender and close the transaction.

The mode in which such an order is carried out by the stockbroker has already been described and need not be restated.

It may be noted that because of the stockbroker's right to close out a short sale after a reasonable time and his expressed desire to do so, this order must be an absolute one to buy at the market price.

(3) The customer can keep quiet and do nothing.

In this case the stockbroker may close out the transaction after a reasonable time[115] has elapsed from his giving notice to[116] the customer of his desire to do so.

No rule can be laid down for determining what a reasonable length of time in this connection is. Each case must be decided on its own circumstances. But it is obviously a short period, not longer in any case than a few days.

As regards the manner in which the stockbroker should act in exercising this right it should be noticed that his right is to close the transaction in the ordinary manner, that is, in the same manner as he would if he had received an order from the customer to do so. And since this right is in law the implied authority every agent has to end his agency after a reasonable time the principles of the law of agency apply generally.

Of the Lender's Right to End the Loan: It has been stated that where the securities are borrowed from a lender upon the usual terms[117] he has the right to end the loan at any time by giving notice[118] to the stockbroker to return the borrowed securities.

If he does, the following courses are open to the stockbroker and his customer:

(1) As already stated, the stockbroker is bound to exercise due care in maintaining the loan and in substituting one lender for another for at least a reasonable time. Hence if such period has *not* elapsed the stockbroker must try to get another lender and with the securities he lends pay off the prior lender and substitute the new one in his place.

(2) If a reasonable time has elapsed from the sale of

the securities the stockbroker has the right to give the customer notice and after a reasonable time has elapsed from the giving of such notice to close the transaction, either with or without an order from the customer to do so, as already described, unless the customer can meantime get another stockbroker who will assume the transaction.

(3) Whether or not a reasonable time has elapsed the stockbroker, if he desires to continue the transaction, can, if he can find a new lender who is willing to take the place of the prior one, substitute him under his authority to do so as already stated.

(4) In any case the stockbroker may be unable to get a new lender. If he is, he should immediately notify the customer. If the customer now orders him to close the transaction or to transfer the transaction to another stockbroker he must do so. If, on the other hand, the customer fails to order the stockbroker to close the transaction or to transfer the transaction to another stockbroker there is nothing for the stockbroker to do but to close out the transaction as soon as possible by buying the securities at the market, returning them to the lender, and accounting to the customer.[119]

ELIOT NORTON.

NEW YORK, October, 1907

NOTES

1. See Prefatory Note.

2. Wherever dealings in securities are common it is usually possible to find purchasers or sellers, lenders or borrowers of any reasonable amount of any kind of security commonly dealt in. This is more particularly the case with such securities as are dealt in on a Stock Exchange than of any others.

3. See the clause numbered 7 on page 12.

4. This transaction is only entered into for speculative purposes, Campbell v. Wright, 118 N. Y. 594; Sistar v. Best, 88 N. Y. 527, 533; Knowlton v. Fitch, 52 N. Y. 288; when the customer's belief is that the price of certain securities is going to decline, Campbell v. Wright, 118 N. Y. 594; White v. Smith, 54 N. Y. 522; Knowlton v. Fitch, 52 N. Y. 288; 23 Am. & Eng. Enc. of Law, 1st ed., 718, 719. Its theory in its briefest form is to sell something you do not own, Knowlton v. Fitch, 52 N. Y. 288; in the hope of making a profit by replacing it at a cheaper price, Hess v. Rau, 95 N. Y. 359; White v. Smith, 54 N. Y. 522; 23 Am. & Eng. Enc. of Law, 1st ed., 719, 720; 25 Am. and Eng. Enc. of Law, 2d ed., 1061; 26 Am. & Eng. Enc.

of Law, 2d ed., 1060; Dos Passos, 200, 201. Except where forbidden by Statute, as in Massachusetts, such a transaction is legal, Hurd v. Taylor, 181 N. Y. 231; cf. Personal Property Law (N. Y.), Sec. 22; and where forbidden by Statute, the prohibition is usually disregarded, Dewey on Contracts for Future Delivery, 14 to 24.

5. The phrase a "short sale" is, when considered, nonsense. A person may be "short" of securities, that is, he may owe them; but obviously a sale cannot be short.

6. The chief American book on Stockbrokers and Stock Exchanges is Mr. John R. Dos Passos's "A Treatise on the Law of Stockbrokers and Stock Exchanges." In many subsequent notes I have simply referred to pages of the 2d edition of this book and also of the American and English Encyclopedia of Law to avoid re-citation of the many authorities collated and cited by Mr. Dos Passos and in the Encyclopedia of Law; and therefore the decisions cited in the notes to the pages of either of these works which are referred to should be considered as referred to as well as the text.

7. Dos Passos, 185. If the stockbroker is acting for a fellow member of his Stock Exchange, he may, if such fellow member is willing, "declare" or "give up" such fellow member in his place as a principal if the stockbroker with whom he is contracting does not object. If the stockbroker is acting for an outsider, there is a custom that he cannot declare or give him up as a princi-

pal and that he should at all times conceal his identity. The custom of dealing in this way has been held to be "reasonable," Whitehouse v. Moore, 13 Abb. Pr. (N. Y.) 42; Peckham v. Ketcham, 10 Abb. Pr. (N. Y.) 220; s. c. 5 Bos. (N. Y.) 506; Horton v. Morgan, 19 N. Y. 170. The stockbroker, however, enjoys no privilege as a witness, and must, if asked, disclose who his customers are, and such other matters within his knowledge relating to their business as are admissible in evidence, Dos Passos, 400–404.

8. He can therefore sue and be sued on his contract although acting for an undiscovered principal, Knapp v. Simon, 96 N. Y. 284; s. c. 86 N. Y. 311; Cobb v. Knapp, 71 N. Y. 348. On the remedies of stockbrokers and their customers as against each other, see Dos Passos, Chap. VII.

9. For a more detailed account of the way stockbrokers deal in the purchase and sale of securities, see an article by me entitled "A Simple Purchase and Sale through a Stockbroker," VIII Harvard Law Review, No. 8, and my essay "On Buying and Selling Securities through a Member of a Stock Exchange," published by Messrs. Baker, Voorhis and Company, New York, 1896; afterwards republished under the same title by S. A. Nelson, New York, 1900.

10. See notes 7 and 8.

11. Cook on Corporations, 4th ed., sec. 445, n. 1 at end.

12. Dos Passos, 250 et seq.

13. Though commonly spoken of as the "market price of the *borrowed* securities," yet by this it is not meant to convey any idea that the identical securities borrowed are referred to, but only securities of the same kind and in the same amount. Hence "the market price of the borrowed securities" at any time is that sum which would then be required to buy securities of the same kind and in the same amount as those borrowed.

14. If the borrower at any time fails in his agreement, the lender can of course call the loan, but before doing so he usually calls upon the borrower to make good his agreement; but this is not legally necessary.

15. Dos Passos, 329.

16. Cook on Corporations, 4th ed., sec. 445, n. 1 at end.

17. Knowlton v. Fitch, 52 N. Y. 288; Hess v. Rau, 95 N. Y. 359.

18. In Dykers v. Allen, 7 Hill (N.Y.) 497; s. c. 42 Am. Dec. 87, Walworth, Ch. said, "There is no doubt that upon an ordinary loan of one hundred shares of the stock of a particular corporation, or of other stock of the like nature, where one share of the stock is just as good as another, it would only be necessary to return the amount of stock in kind. *The loan in such a case is in substance a sale* to be repaid in kind and quantity, and the title to the fungibles loaned is immediately transferred to the borrower; whereas upon the loan of specific articles to be returned in specie, the title remains in the lender, and the borrower is only

entitled to the temporary use thereof," and cited 3 Erskine's Inst., tit. I, 18. See also Bradley v. Merick, 25 Hun, 272; Benjamin on Sales, Kerr's ed., page *2, note 6 on pp. 6, 8, 12, and *2, Sec. 2; and 23 Am. & Eng. Enc. of Law, 1st ed., 719. In spite of these authorities it seems to me a mistake to call a loan of securities a sale. It does not make much difference but the parties call it a loan and think it a loan. Moreover, if in some respects it resembles a sale in others it is totally irreconcilable with the idea of a sale, to wit: in the security given to the lender and in the paying of interest by him. Besides, if the question merely turns on the transfer of title, why not call a loan of cash a sale of cash?

19. Caswell v. Putnam, 120 N. Y. 153; Stewart v. Drake, 46 N. Y. 449; Horton v. Morgan, 19 N. Y. 170; Ingraham v. Taylor, 58 Conn. 503; Dos Passos, 253.

20. If any statement of the usual terms of Stock Exchange loans of securities exists in print it is not of easy access, and has not been found by me. But for a few cases where such loans were considered, see Hess v. Rau, 95 N. Y. 359; Cameron v. Durkheim, 55 N. Y. 425; White v. Smith, 54 N. Y. 522; Knowlton v. Fitch, 52 N. Y. 288, revg. 48 Barb., 593; see also 23 Am. & Eng. Enc. of Law, 1st ed., 719; Dos Passos, 327; Cook on Corporations, 4th ed., Sec. 445, n. 1, at foot.

21. The word "order" will be used throughout this article as signifying only an order in the regular form.

The word "order" is commonly used by stockbrokers as signifying any kind of a proposition relating to the purchase or sale of securities.

22. These customs, technical words, and technical meanings apply, *mutatis mutandis*, to other things besides orders in the regular form; for instance, to the wording of notices (see pages 28 and 29) given by stockbrokers to their customers; but for the purpose of this essay the exact scope of these customs need not be considered.

23. When an order is not in the regular form it may be an indication that the customer may not understand or even know of the customs set out in the text, but if technical words are used in an order the customer cannot afterwards claim that he intended them to have other than their technical meaning, Dos Passos, 206, 220, and Chap. IV.

24. See subdivision entitled "First, Of Purchases and Sales" on page 7 of the text.

25. For two cases illustrating the nature and extent of this custom, see Rosenstock v. Tormey, 32 Md. 169; and Porter v. Wormser, 94 N. Y. 431.

26. Fairbairn v. Rausch, 104 App. Div. (N. Y.) 259. This case held that an order to sell "at the market" means that the sale shall be made at the best price obtainable at the time the order is executed and not at the price prevailing at the time the order is given.

27. Dos Passos, 208, 327; Mechem on Agency, Sec. 362, 946.

28. Campbell v. Wright, 118 N. Y. 594; White v. Smith, 54 N. Y. 522; 26 Am. & Eng. Enc. of Law, 2d ed., 1055; Cook on Corporations, 4th. ed., Sec. 445.

29. For a large collection of cases on the interpretation of the engagements of stockbrokers according to custom and an intelligent discussion of this question, see Dos Passos, Chap. IV., p. 410.

30. The authority to borrow may be given separately and not until the stockbroker has contracted to sell the securities, see page 14 at top.

31. In an article in the Harvard Law Review, Vol. VIII, No. 8, I stated that this offer was made in consideration of the stockbroker *contracting* as he was authorized to do. I was wrong. The text here is right.

32. Hess v. Rau, 95 N. Y. 359, 363; Dos Passos, 227; Mechem on Agency, Sec. 365, 977.

33. Dos Passos, 394, et seq. Cf. "Where there is no express agreement as to the compensation of an agent, usage, if any, will determine what he should receive," United States v. Duval, Gilp. 356; cf. Morgan v. Mason, 4 E. D. Smith (N. Y.) 636; Mechem on Agency, Sec. 963.

34. Thus the question of whether the stockbroker has earned his commission is easy of determination, and the difficulties which arise with it in the case of real estate brokers do not exist, Mechem, Sec. 965.

35. Dos Passos, 206.

36. See page 35.

37. Dos Passos, 209, n. 5.

38. That is, "bound" in the sense of bound by contract; of course the stockbroker is bound by the duties which the law imposes on him as an agent. Cf. Knowlton v. Fitch, 52 N.Y. 288, and Markham v. Jaudon, 41 N.Y. 235.

39. Allen v. McConihe, 124 N. Y. 342; Campbell v. Wright, 118 N. Y. 594; Gruman v. Smith, 81 N. Y. 25; Scott v. Rogers, 31 N. Y. 676; 26 Am. & Eng. Enc. of Law, 2d ed., 1055; Cook on Corporations, 4th ed., Sec. 448.

40. Allen v. McConihe, 124 N. Y. 342; Gregory v. Wendell, 40 Mich. 432.

41. Gillett v. Whiting, 120 N. Y. 402; Harris v. Tumbridge 83, N. Y. 92; Taussig v. Hart, 49 N. Y. 301; Brass v. Worth, 40 Barb. (N. Y.) 648; Dos Passos, 212; 26 Am. & Eng. Enc. of Law, 2d ed., 1056.

42. Baker v. Drake, 53 N. Y. 211; Hanks v. Drake, 49 Barb. (N. Y.) 186; Stewart v. Harris, 101 App. Div. (N. Y.) 181.

43. Harris v. Tumbridge, 83 N. Y. 92; Dos Passos, 180, 181, 198–200, 218; Mechem on Agency, Sections 454, 472, 951–954; 26 Am. & Eng. Enc. of Law, 2d ed., 1056. It should be also noted that stockbrokers besides being agents are, in some respects at least, "fiduciaries," Waters v. Marvin, 12 Daly (N. Y.) 445; Dos Passos, 198–200, 779 n. 4; see also McBurney v. Martin, 6 Robt. (N. Y.) 502; Mann v. Sands, 2 City Ct. (N. Y.) Rep. 25; Martin v. Gross, 22 N. Y. State Rep. 439.

44. Haight v. Haight & Freese Co., 46 Misc. (N. Y.) 501.

45. Williams v. Hays, 143 N. Y. 442, on pp. 453–454; Isham v. Post, 141 N. Y. 100; Dos Passos, 218.

46. Murray v. Beard, 102 N. Y. 505; Dos Passos, 218; Mechem on Agency, Sec. 936.

47. Porter v. Wormser, 94 N. Y. 431, 447; Levy v. Loeb, 89 N. Y. 386, s. c. 85 N. Y. 365; s. c. 47 N. Y. Super. Ct. 61; Taussig v. Hart, 58 N. Y. 425; s. c. 49 N. Y. 301; Prout v. Chisholm, 21 App. Div. (N. Y.) 54; Evans v. Wrenn, 93 App. Div. (N. Y.) 346; Dos Passos, 365–385.

48. Gardner v. Ogden, 22 N. Y. 327.

49. Francis v. Kerker, 85 Ill. 190; Solomon v. Pender, 3 H. & C. 639.

50. Porter v. Wormser, 94 N. Y. 431; Gardner v. Ogden, 22 N. Y. 327.

51. Taussig v. Hart, 58 N. Y. 425; Gardner v. Ogden, 22 N. Y. 327; Conner v. Black, 24 S. W. (Mo.) Rep. 184.

52. Robinson v. Mollett, L. R. 7 H. L. App. Cases, 802.

53. That is, it does not include the performance of the contract or contracts to sell by the delivery of the securities sold and the receipt of the purchase price.

54. This custom is opposed to the rule that an authority is good till countermanded, if such a rule exists; cf. Dickenson v. Tilwall, 1 Stark. 128, s. c. 4 Campb. 279.

55. Allen v. McConihe, 12 N. Y. Supp. 232. As to what phrase will give him a discretionary power: "Do

the best you can for me," see Cowell v. Loud, 135 Mass. 41; "You must take care of yourselves," see Cameron v. Durkheim, 55 N. Y. 425; cf. also Billingslea v. Smith, 77 Md. 504.

56. Dos Passos, 206 et seq.; Cook on Corporations, 4th ed., sec. 448.

57. Neither good intentions on the stockbroker's part nor even actual benefit to the customer furnish any excuse in law for failure to carry out orders, Allen v. McConihe, 12 N. Y. Supp. 232.

58. Until the stockbroker has done some thing to bind the customer, viz. "execute" the order, an order can be revoked, Dos Passos, 210, 211. The customer is bound, however, to indemnify the stockbroker for any expense or loss he may have incurred. This, of course, does not include his unearned commissions. On the general principles of law governing the revocation of orders given to brokers, see Sibbald v. The Bethlehem Iron Co., 83 N. Y. 378; Mechem on Agency, Sections 204, 968.

59. Green v. Johnson, 90 Pa. St. 38; Gregory v. Wendell, 40 Mich. 432; Rosenstock v. Tormey, 32 Md. 169.

60. Mechem on Agency, Section 944.

61. Sims v. May, 16 N. Y. St. Rep. 780.

62. Marye v. Strouse, 5 Fed. Rep. 483; Evans v. Wrenn, 93 App. Div. (N. Y.) 346; Dos Passos, 208.

63. Finney v. Gallaudet, 15 Daly (N. Y.) 66; Hoffman v. Livingstone, 46 N. Y. Super. Ct. 552; Cameron v.

Durkheim, 55 N. Y. 425; Dos Passos, 213. The stockbroker is permitted to give evidence that a notice contained errors, Porter v. Wormser, 96 N. Y. 431.

64. Minor v. Beveridge, 141 N. Y. 399.

65. Hoffman v. Livingstone, 46 N. Y. Superior Court, 552.

66. White v. Smith, 54 N. Y. 522; Knowlton v. Fitch, 52 N. Y. 288. If the order discloses that the stockbroker is expected to borrow the securities ordered to be sold in order to deliver them to the purchaser it would be presumptively want of care on his part if after contracting to sell the securities he should find he could not borrow them.

Note also that if prior to the time of delivery the securities sold were repurchased and such repurchased securities delivered to the purchaser on the original sale there would be no need for borrowing any securities.

67. The transaction is equivalent to selling borrowed securities, or as sometimes said, to selling securities the customer does not own, see Hess v. Rau, 95 N. Y. 359; Knowlton v. Fitch, 52 N. Y. 288.

68. Campbell v. Wright, 118 N. Y. 594, 599; Hess v. Rau, 95 N. Y. 359; White v. Smith, 54 N. Y. 522, 526.

69. Hess v. Rau, 95 N. Y. 359; White v. Smith 54 N. Y. 522. See page 41 at middle.

70. Cameron v. Durkheim, 55 N. Y. 425.

71. See ante pages 8 to 13. It is to be noted that none

of these usual terms conflict with the restrictions above stated on the stockbroker's authority to borrow.

72. Knowlton v. Fitch, 52 N. Y. 288, 294; 23 Am. & Eng. Enc. of Law, 1st ed., 719.

73. See note 4. The stockbroker is said "to put the customer short," and the customer is said "to go short" and "to be short." The word short is here used in the sense of "wanting and owing" as in the phrase "short in one's accounts."

74. White v. Smith, 54 N. Y. 522; 23 Am. & Eng. Enc. of Law, 1st ed., 719, 720.

75. Hess v. Rau, 95 N. Y. 359.

76. Because of this it is part of due care in maintaining the loan to make substitutions until at least a reasonable time has elapsed from the commencement of the transaction if the stockbroker can do so.

77. See (4) on page 9.

78. Dos Passos, 182, 194, 337, n. 4.

79. Dos Passos, 194.

80. These include all interest in the shape of dividends, coupons or otherwise, and all bonuses or accretions which may be paid on the securities sold, for these must in turn be paid to the lender; for, otherwise, having loaned his securities, he would not receive them, see page 11.

81. The price at any time is determined by the price the securities could be purchased for on the Exchange on which the transaction is performed, and this in the case of

an "active stock" is determined by the last official quotation of a transaction in such stock.

82. To illustrate, suppose a margin of $1,000 be put up on a sale of 100 shares of securities for $95 per share of the par value of $100 or $9,500 total price, and that the price then rises to $98 per share or $9,800 as the total value of the 100 shares. The margin would be treated as reduced to $700.

83. 23 Am. & Eng. Enc. of Law, 1st ed., 720.

84. If the price then went below par the customer would not, strictly speaking, be allowed to draw out any more, for his margin should always remain at the $1,000 originally deposited, but he might be allowed to draw out some money "on account of prospective profits."

85. On the use the stockholder can put the margin to, see pages 39 at foot and 40. Cf. Waters v. Marvin, 12 Daly (N. Y.) 445; Dos Passos, 198–200, 779, n. 4; McBurney v. Martin, 6 Robt. (N. Y.) 502, Mann v. Sands, 2 City Ct. (N. Y.) Rep. 25; Martin v. Gross, 22 N. Y. State Rep. 439.

86. It carries into practical effect the customer's offer to indemnify the stockbroker, as to which see ante page 20 under 2.

87. That is, they are charged against it and paid out of it, and then the customer called to make good his margin.

88. To illustrate, suppose the securities are to be kept

with the lender at the market. At the beginning suppose par was the market price. Then suppose the securities rise to 105. Five hundred dollars will have to be paid the lender. But the customer's margin has been reduced by the rise by five hundred dollars, and he has to give that amount to the stockbroker to make it good.

89. 23 Am. & Eng. Enc. of Law, 1st ed., 720, and 26 Am. & Eng. Enc. of Law, 2d ed., 1060.

90. That is, the customer, who is the "undiscovered" principal in the loan

91. Haight v. Haight & Freese Co., 46 Misc. (N. Y.) 501; Dos Passos, 219, 398; 26 Am. & Eng. Enc. of Law, 2d ed., 1056.

92. See note 9.

93. This is similar to the regular form used when securities are ordered sold, see page 13, except that the word "buy" takes the place of "sell."

94. See pages 14 et seq.

95. See note 9. And cf. p. 18 under "The Legal Nature of an Order."

96. As stated on page 41, there is found in the stockbroker's agency to borrow an implied expression of willingness on the part of the stockbroker to act as the customer's agent in ending the loan, so it would be a breach of his duties as agent to refuse to take an order to buy the securities required to end the loan.

97. The interest paid by the lender on the moneys de-

posited with him (see clause 5 on page 11) is retained by the stockbroker as a kind of perquisite. In the absence of any agreement to this effect he is not justified in law in doing so, and no custom would be held to justify him.

98. Hess v. Rau, 95 N. Y. 359.

99. Rogers v. Wiley et al., 131 N. Y. 527, s. c. 30 N. Y. St. Rep. 231, s. c. 14 N. Y. Supp. 622; Campbell v. Wright, 118 N. Y. 594; Cameron v. Durkheim, 55 N. Y. 425; White v. Smith, 54 N. Y. 522.

100. Cameron v. Durkheim, 55 N. Y. 425.

101. Campbell v. Wright, 118 N. Y. 594; Cameron v. Durkheim, 55 N. Y. 425.

102. Dos Passos, 336, 337.

103. Lazare v. Allen, 20 App. Div. (N. Y.) 616. When the customer complies with a demand for more margin it is called "keeping his margin good."

104. 55 N. Y. 425, 429.

105. Except "where the facts are undisputed," when it is a question for the Court, Wright v. Bank of the Metropolis, 110 N. Y. 237; Burnham v. Lawson, 118 App. Div. (N. Y.) 389.

106. Generally, on this demand, Dos Passos, 334–346; 26 Am. & Eng. Enc. of Law, 2d ed., 1061.

107. Campbell v. Wright, 118 N. Y. 594; Cameron v. Durkheim, 55 N. Y. 425, 427; Wright v. Smith, 54 N. Y. 522; Knowlton v. Fitch, 52 N. Y. 288; 26 Am. & Eng. Enc. of Law, 2d ed., 1061.

108. Rogers v. Wiley, 131 N. Y. 527, s. c. 38 N. Y. St. Rep. 231, s. c. 14 N. Y. Supp. 622; Hess v. Rau, 95 N. Y. 359; White v. Smith, 54 N. Y. 522; Knowlton v. Fitch, 48 Barb. (N. Y.) 593; Lazare v. Allen, 20 App. Div. (N. Y.) 616, but see Corbett v. Underwood, 83 Ill. 324; Rogers v. Wiley, 131 N. Y. 527.

109. Lazare v. Allen, 20 App. Div. (N. Y.) 616; Sterling v. Jaudon, 48 Barb. (N. Y.) 459.

110. Generally on this notice see Dos Passos, 347–356 and 23 Am. & Eng. Enc. of Law, 1st ed., 711. When stocks are carried on a margin they constitute a pledge, and to sell a pledge requires a notice stating the time and place of sale which must be at public auction; bearing this difference in mind, what has been laid down in cases and text-books relating to the notice and the time which must elapse before the transaction can be closed in cases where securities were being carried, applies to the notice, etc., in cases of selling securities short.

111. That is, it is a term of the agreement under which the margin is deposited.

112. Hess v. Rau, 95 N. Y. 359; White v. Smith, 54 N. Y. 522; 26 Am. & Eng. Enc. of Law, 2d ed., 1060.

113. That is, the stockbroker is fully protected by virtue of the margin and the agreement under which it is deposited.

114. Hess v. Rau, 95 N. Y. 359; White v. Smith, 54 N. Y. 522. This notice must be served upon the custo-

mer in the same manner that the notice of sale for default in furnishing margin is served.

115. Cameron v. Durkheim, 55 N. Y. 425.

116. Hess v. Rau, 95 N. Y. 359; Cameron v. Durkheim, 55 N. Y. 425; White v. Smith, 54 N. Y. 522.

117. If the stockbroker lends securities he is carrying for a customer such customer may cause the end of the loan by ordering the securities sold or by "taking up" the securities or by refusing to allow them to be loaned. In such case what is stated in the text under (1), (2), (3), and (4) applies without change. If the stockbroker lends *his own securities* his interests as lender and as stockbroker for the customer who has "sold short" may be opposed, which is a sufficient reason for believing that the law would not approve of a stockbroker lending his own securities.

118. Where the lender calls the loan the borrowed securities must be returned within a reasonable time, which, when not fixed by the contract under which the securities are borrowed or by the rules of a Stock Exchange, is no more than to the close of banking hours of the day following the day on which it is called. Hence any of the alternative courses of action mentioned under (1), (2), (3), and (4) in the text must be performed within this period.

119. Speculators are divided into those who are buying for a (the) rise and those who are selling for a (the) decline. There are two ways by which the latter can be done: that described in the text, which is the usual way;

the other by selling securities which the seller does not own for some "future delivery," by which time the seller hopes to have acquired the securities at a price below that which he sold them for, which is not commonly engaged in. Persons who engage in selling for the decline are known as "bears" (23 Am. & Eng. Enc. of Law, 1st ed., 700, n. 5, and 719), in contradistinction to "bulls," who are those who engage in buying for a rise. To "bear" a security is to sell such amounts of it, whether owned by the seller or borrowed for delivery or sold for future delivery, as will have a tendency to depress its price.

ELIOT NORTON.

NEW YORK, October, 1907.

Ex. C. A. J.
1/9/08

L'ENVOI

"He that sells what he hathe notte
Is certain sure to go to Potte;
But he as only sells what's his'n
Need never fear a debtor's prison."

Old Rhyme.